

Message Text

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SUBJECT: PROSPECTS FOR ZAMBIA'S ECONOMY

REF: STATE 047174

1. DOMINANT FACTOR AFFECTING ZAMBIAN ECONOMY REMAINS PRICE OF COPPER, PRODUCTION AND EXPORT OF WHICH NORMALLY ACCOUNTS FOR 40 PERCENT OF GDP, HALF OF GOVERNMENT REVENUES, AND 90-95 PERCENT OF FOREIGN EXCHANGE EARNINGS. IN PAST, ZAMBIA HAS COUNTED ON LARGE TRADE SURPLUS FROM COPPER EXPORTS TO FINANCE DEVELOPMENT PROJECTS AND PAYMENTS FOR NON-FACTOR SERVICES. IN 1973, SURPLUS AMOUNTED TO \$625 MILLION; IN 1974 ABOUT \$550 MILLION. DURING 1975, HOWEVER, IF COPPER PRICE REMAINS AROUND PRESENT \$1300 PER TON, SURPLUS FROM COPPER WILL BE BARELY ENOUGH TO COVER PROJECTED IMPORTS.

2. DECLINING FROM \$371 MILLION IN JUNE 1974, ZAMBIA'S FOREIGN
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EXCHANGE HOLDINGS ON JANUARY 1, 1975, STOOD OFFICIALLY AT \$200

MILLION; THEY ARE NOW NEAR \$100 MILLION ACCORDING TO UNOFFICIAL SOURCES. OUTLOOK IS FOR FURTHER EROSION.

3. TAX REVENUES FROM MINING IN 1974 WERE \$511 MILLION, AN UNUSUALLY HIGH FIGURE BECAUSE OF RECORD COPPER PRICES FIRST HALF OF YEAR. ANTICIPATED MINERAL REVENUE FOR 1975 IS DOWN TO \$203 MILLION. THIS NOT A DISASTROUS CHANGE COMPARED TO \$248 MILLION AVERAGE SINCE 1969, NOR ANYWHERE NEAR THE LOWS OF 1971 AND 1972. BUT IT CLEARLY QUITE INSUFFICIENT FOR A BUDGET WHICH HAS MORE THAN DOUBLED IN SIX YEARS AND IS NOW SADDLED WITH RECURRENT EXPENDITURES OF \$803 MILLION (WITH SALARIES, SUBSIDIES, AND FIXED OPERATING EXPENDITURES BEING INFLEXIBLE ELEMENTS OF BUDGET). EVEN WITH ESTIMATED RECEIPTS OPTIMISTICALLY AT OR ABOVE 1974 LEVEL, AND WITH \$212 MILLION IN PROPOSED INTERNAL AND EXTERNAL FINANCING, PROJECTED CURRENT ACCOUNT DEFICIT IS \$243 MILLION.

4. SOME DOMESTICALLY FINANCED INVESTMENT AND DEVELOPMENT PROJECTS MAY BE THREATENED, THOUGH IT TOO EARLY TO DRAW FIRM CONCLUSIONS THIS REGARD. PROSPECTIVE NEGATIVE IMPACT ON ALREADY POOR EMPLOYMENT PICTURE NOT PROPITIOUS. AT BEST, IT CANNOT BE EXPECTED THERE WILL BE IMPROVEMENT ON RECENT YEARS WHEN, DESPITE FAVORABLE ECONOMIC CONDITIONS, AVERAGE OF ONLY ABOUT 16,000 MODERN SECTOR JOBS WERE CREATED ANNUALLY IN FACE OF ESTIMATED NEED FOR 67,000.

5. HIGH PETROLEUM COSTS, WHILE DISTURBING DRAIN ON FOREIGN EXCHANGE AND GOVERNMENT REVENUES, WILL HAVE LESS SEVERE IMPACT ON ZAMBIAN ECONOMY THAN LOW COPPER PRICE. ACCORDING TO MINISTER OF PLANNING AND FINANCE, COST OF OIL IMPORTS (EXCLUDING LUBRICANTS) ROSE FROM LESS THAN \$26 MILLION IN 1973 TO \$61 MILLION IN 1974 AND ESTIMATED \$80 MILLION IN 1975. IMF CALCULATES 1976 FIGURE AT \$126 MILLION. PETROLEUM ACCOUNTS FOR ONLY ABOUT 23 PERCENT OF COUNTRY'S ENERGY REQUIREMENTS. AS PERCENT OF IMPORT BILL, PETROLEUM HAS DOUBLED TO 10 PERCENT BETWEEN 1973 AND 1975. HIGH OIL PRICE HAS OF COURSE HAD INDIRECT IMPACT THROUGH ITS INFLUENCE ON GENERAL WORLD INFLATION. ALMOST ALL ZAMBIAN IMPORT COSTS ARE UP MARKEDLY; ZAMBIAN FREIGHT AND TRANSPORT BILL EXPECTED TO REACH \$187 MILLION IN LIMITED OFFICIAL USE

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1975 COMPARED TO \$127 MILLION IN 1973. LIKE ZAIRE, ZAMBIA HAS SOUGHT BUT GOTTEN NO DIRECT RELIEF FROM ARAB OIL PRODUCERS.

6. ZAMBIAN RESPONSE TO ITS ECONOMIC PROBLEMS HAS BEEN TO TEMPORIZE, RATHER THAN COME FIRMLY TO GRIPS WITH THE NEED TO RETRENCH. SEVERE FISCAL REMEDIES WERE ANTICIPATED, BUT NOT FORTHCOMING IN THE 1975 BUDGET WHICH WAS HIGHLY

POLITICAL IN DESIGN.

7. PRESIDENT KAUNDA AND HIS GOVERNMENT ARE DEEPLY PREOCCUPIED WITH SOUTHERN AFRICAN POLITICAL DEVELOPMENTS AND A DAMPER IS BEING KEPT ON ANY DOMESTIC DISSENSION WHICH MIGHT ARISE FROM ECONOMIC AUSTERITY MEASURES. MOREOVER, ZAMBIANS ARE CONFIDENT THEY CAN REPLY A GREAT DEAL ON FOREIGN BORROWING TO SEE THEM THROUGH AND POSTPONE DOMESTIC HARDSHIPS.

8. PROSPECTS FOR EXTERNAL BORROWING INDEED APPEAR GOOD OVER NEAR TERM AT LEAST, ESPECIALLY SINCE ZAMBIA ENJOYS MERITED REPUTATION AS GOOD CREDIT RISK AND IS IN COMFORTABLE 5 PERCENT DEBT SERVICE RATIO POSITION. LEADING AMERICAN AND EUROPEAN BANKS, WHICH PROVIDED \$150 MILLION TO ZAMBIA ONLY 18 MONTHS AGO, ARE CURENTLY SEEKING ARRANGE ADDITIONAL \$200 MILLION FOR MINING INDUSTRY.

9. GRZ ANTICIPATES MAKING UP MOST OF BUDGET REVENUE SHORTFALL THROUGH INCREASED AND NEW SALES AND EXISE TAXES AS WELL AS DOMESTIC AND FOREIGN BORROWING. IF THESE MEASURES SUCCESSFUL, REVENUE DECLINE FROM 1974 LEVEL IS FORECAST AT MERE 5-6 PERCENT, BUT THIS SEEMS OVERLY OPTIMISTIC. A FEW CONTROLLED PRICES HAVE BEEN RAISED (BEER, SUGAR, GASOLINE), A SELECTIVE 10 PERCENT SALES TAX HAS BEEN ADOPTED, AND A MOVE TO REDUCE NON-ESSENTIAL IMPORTS IS UNDERWAY (UNFORTUNATELY IN A MANNER CREATING UNCERTAINTY AND THREATENING ESSENTIAL SUPPLY). TO RESTRAIN THE FOOD IMPORT BILL AND POSSIBLY REDUCE IT, NEW REMITTANCE RIGHTS AND SUBSIDY PAYMENTS HAVE BEEN GRANTED EXPATRIATE COMMERCIAL FARMERS WHO PRODUCE BULK OF MARKETABLE SURPLUSES. MORE MEASURES ARE TO BE EXPECTED, BUT THE INCLINATION TO POSTPONE ACTION APPEARS TO REMAIN STRONG.
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10 ZAMBIA SHOULD BE ABLE TO WEATHER 1975 WITHOUT EXTREME DIFFICULTY, WHILE PRESERVING ITS DOMESTIC PEACE AND TRANQUILITY, IF FOLLOWING CONDITIONS MET: US AND WORLD ECONOMY PICKS UP IN THIRD QUARTER, COPPER PRICE DOES NOT WORSEN APPRECIABLY BUT RATHER STENGHTENS, MAJOR WIDESPREAD VIOLENCE DOES NOT ERUPT IN SOUTHERN AFRICA, SOME DOMESTIC AUSTERITY INTRODUCED, AND ADEQUATE EXTERNAL LOANS ARE FORTHCOMING.
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